Supreme Court, U. S.
FILED
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MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

No. 79-1439

WENDELL REICH AND ROBERT PAUL,
Petitioners,

versus

REED TOOL COMPANY,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF TEXAS

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1979

No.

WENDELL REICH AND ROBERT PAUL,
Petitioners,

versus

REED TOOL COMPANY,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF TEXAS

Petitioner respectfully prays that a writ of certiorari issue to review the final order of the Supreme Court of the State of Texas entered on the 5th day of December, 1979, and the order of the Supreme Court of the State of Texas denying Application for Writ of Error with the notation "no reversible error", thus affirming the opinion of the Court of Civil Appeals for the Fifth Supreme Judicial District of the State of Texas.

OPINION BELOW

The orders of the courts below are appended hereto, infra at Pages 1a, 16a and 17a.

JURISDICTION

The jurisdiction of this court is invoked under 28 U.S.C. §1257(3).

QUESTIONS PRESENTED

(1) Does the Federal Doctrine of Patent Misuse apply equally to the sale of an application for a patent as it does to the sale of a patent?

(2) Does a patent application have such monopolistic power that an inventor can condition its assignment in violation of the Patent Misuse Doctrine?

CONSTITUTIONAL AND REGULATORY PROVISIONS INVOLVED

The principal constitutional provision involved is Article One, Section Eight of the United States Constitution.

STATEMENT OF THE CASE

This is a suit for commissions and an accounting growing out of a contract for the sale of a patent appli-

cation covering certain rotary earth drilling equipment. The Court of Civil Appeals for the Fifth Supreme Judicial District of Texas and the Texas Supreme Court in approving the holding of the Court of Civil Appeals, has held that the Federal Doctrine of Patent Misuse applies to the sale of a patent application. The opinion of the Court of Civil Appeals appended hereto at Pages 1a-16a correctly states the nature and result of the suit.

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

This is truly a case of first impression. The question presented is really quite simple — does the doctrine of patent misuse apply to the sale of a patent application? The trial court, Court of Civil Appeals, and Supreme Court have all answered in the affirmative despite the admission by the Court of Civil Appeals that "on this question the authorities are inconclusive". The implications of such a holding are staggering and will, hopefully, be explored with clarity herein so that the fallacy of such an answer may be exposed.

In order to answer our question it is necessary first to understand what patent misuse is. The Court of Civil Appeals in its opinion correctly summarized misuse as:

> ". . . a doctrine developed by the Federal courts to prevent the holder of a patent from using his statutory and constitutional monop-

> oly power to coerce economic benefits not directly flowing from the rights granted by the patent."

It appears elementary that in order for this definition to apply there must, in fact, be a patent. The use of the words "statutory and constitutional monopoly" presupposes the existence of a patent. Where there is a right there is a correlative responsibility. When a patent has issued, its holder is entitled to a monopolistic right to make, sell or use the patented product. However, the holder has the correlative responsibility not to use the leverage created by his patent protection to extract an agreement overreaching the bounds of that protection. *An application for a patent is not a patent.* A patent application carries with it *absolutely none* of the protective monopolistic features that flow with the grant of a patent. A patent application carries with it nothing more than the hope that a patent will issue. Thousands upon thousands of applications are turned down flat. There is no *right* to any monopolistic protection, thus the correlative *responsibility* not to misuse the protection does not exist.

Petitioners Wendell Reich and Robert Paul sold to Respondent Reed Tool Company a patent application along with a going business and the expertise of Reich. They did not have a patent. Having divested themselves of the application, they gave away all ties to the patent that subsequently issued. If it can be said that

Petitioners had the *responsibility* in their sale to Respondent not to negotiate for commissions on products not covered by their patent application, where was the correlative *right* of monopoly that they were giving up? It simply did not exist. Thus, logic tells us that the doctrine of patent misuse does not apply to the sale of a patent application as opposed to the sale of an issued patent.

It further appears that we must find our answer in logic since the case law does not provide it for us. Not only are the authorities "inconclusive" upon the precise point presented herein, they are nonexistent. In short, no Federal court has written upon our question nor has any state court addressed the issue. It is submitted that the reason for such darth of authorities is that the answer is so fundamental. Before there can be misuse, there must be a patent.

Numerous cases were cited and distinguished by the parties in their briefs to the Court of Civil Appeals and by that Court in its opinion, including *Zenith Radio Corporation vs. Hazeltine Research, Inc.*, 395 U.S. 100 (1969); *Mutchnik vs. M. S. Willett, Inc.*, 274 Md. 610, 337 A.2d 72 (Md. 1975); *Richards vs. Liquid Controls Corporation*, 26 Ill. App. 3d 111, 325 N.E.2d 775, 784 (App.Ct. 1975); *Key Pharmaceuticals, Inc. vs. Lowey*, 373 F.Supp. 1190, 1193 (1974); *Krampe vs. Ideal Industries, Inc.*, 347 F.Supp. 1384, 1386-87 (N.D. Ill. 1972); and *Anderson Company vs. Trico Products Corp.*, 327 F.Supp. 834, 838 (W.D.N.Y. 1964).

Suffice it to say that all of the above cases involved licensing agreements as opposed to the outright sale or assignment of a patent or patent application. A licensing agreement is distinguished from a sale or assignment in that under the former the licensee is granted the right to make, use or sell the patented product for a period of time while the patent itself remains with the licensor who is paid royalties. Under the latter, there is a complete divestiture of title to the patent. Each of the above cited cases involved a form of misuse and in each case a patent was either owned by or subsequently issued to the *licensor* who was insisting upon enforcing alleged overreaching provisions in the licensing agreement. In our case, however, Petitioners *never* owned the patent in question and the parties never contemplated that they would because, under their contract, Petitioners assigned all their rights in the application.

Upon this point, the Court of Civil Appeals' treatment of the *Krampe* case (supra) bears scrutiny. After mentioning the "inchoate" rights referred to in that decision, the Court of Civil Appeals quoted therefrom as follows:

> "Accordingly, this court finds that plaintiff's use of the rights which he possessed in his invention to secure an additional right to which he was not entitled, *combined with* his maintaining the objectionable terms of the contract after these rights had ripened into a

> patent monopoly, constitutes misuse of his patent for the cable stripper."

It thus appears that the Court of Civil Appeals recognized a two-fold test for determining misuse in a case involving a questionable provision in an agreement negotiated before a patent issued but sought to be enforced after the issuance of the patent by the licensor. However, the court simply ignored this two-fold test when it stated in the last paragraph of Section 1 of its opinion:

> "Neither is it essential to the misuse doctrine that the inventor continue to use the leverage of his monopoly after the patent has issued."

It is respectfully submitted that the Honorable Court of Civil Appeals either forgot what it had just said or reached an illogical result and tried to write to that result.

There are some additional implications that arise from the holding of the trial court and Court of Civil Appeals and the Supreme Court of the State of Texas. What if a patent had not issued to Reed Tool Company? Would not the agreement in question have then been enforceable? What if Petitioners had not had an application on file but Reed subsequently obtained a patent on the invention? Would there have been any

stronger guarantee of success in obtaining the patent merely because an application was already on file? It seems obvious that the answer to these questions is that we must look at the facts as they exist at the time of the agreement in question and then determine to whom the monopoly of a patent was granted before a question of misuse can be answered.

There are two words in patent misuse — "patent" and "misuse". "Patent" involves a monopolistic *right*. "Misuse" can be viewed as the correlative *responsibility* not to overextend that right. Both must exist at the same time in the same individual before patent misuse exists. An arm's length contract negotiated between two competent individuals should not be disturbed when *both* elements do not exist. The rationale for the doctrine does not exist under such circumstances. Petitioner Wendell Reich and Robert Paul at no time have had the right — the patent. Our system of justice and democracy does not impose on them the responsibility in absence of such right.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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LARRY CAIN

CERTIFICATE OF SERVICE

I, the undersigned, do hereby certify that three copies of the above and foregoing Petition for a Writ of Certiorari to the Supreme Court of the State of Texas have been mailed to Mr. A. H. Evans, of Vinson & Elkins, First City National Bank Building, Houston, Texas 77002, and to Mr. Rayburn Nall, 113 West Mulberry, Suite 109, Sherman, Texas 75090, attorneys of record for Respondent, this ____ day of March, 1980.

LARRY CAIN

APPENDIX "A"

OPINION OF THE
COURT OF CIVIL APPEALS,
FIFTH SUPREME JUDICIAL DISTRICT
OF TEXAS AT DALLAS,
OPINION BY CHIEF JUSTICE GUITTARD

COURT OF CIVIL APPEALS
FIFTH SUPREME JUDICIAL DISTRICT OF TEXAS
AT DALLAS

No. 19812

WENDELL REICH AND ROBERT PAUL,
Appellants,

versus

REED TOOL COMPANY,
Appellee.

FROM A DISTRICT COURT
OF GRAYSON COUNTY, TEXAS

BEFORE CHIEF JUSTICE GUITTARD
AND JUSTICES STOREY AND HUMPHREYS

OPINION BY CHIEF JUSTICE GUITTARD

MAY 14, 1979

This suit was brought for commissions alleged to be due under a written contract for sale of an invention and the inventor's rights to a patent, which had been applied for but not issued when the contract was signed. One of the defenses was that the inventor had "misused" the patent by requiring the purchaser to pay commissions on sales of equipment not covered by the patent applied for. After a trial and verdict, the judge disregarded findings favorable to plaintiffs and rendered judgment for defendant based on a single finding relating to the defense of patent misuse. Plaintiffs appeal on the ground that the court erred in applying the "patent misuse" doctrine under the circumstances of this case and also on the ground that the issue of misuse was not correctly submitted. We affirm on the ground that the doctrine applies, even though the inventor's right to the patent was only prospective when the contract was signed, and that the finding on the issue in question is sufficient, in the absence of objection, to support the judgment.

The inventor in this case was plaintiff Wendell Reich, who was in the business of making and selling rotary earth-drilling equipment for water wells. Reich had invented a type of mobile rotary drill and had applied for a patent. While application for this patent was pending, Reich and plaintiff Robert Paul, a business associate, entered into negotiations with Texoma, Incorporated, a subsidiary of defendant Reed Tool Company, for sale of this invention and the inventor's rights under the patent application. These negotiations resulted in the contract in question. The contract provides for sale of the invention and prospective patent rights in consideration of certain payments, including the commissions now claimed. These commissions are payable at specified rates on sales of the "product," defined in the contract as including not only the invention covered by the claims of the patent application, but also other types of rotary earth-drilling equipment. The crucial language of the definition covering such other types of equipment is paragraph (1)(d), as follows:

> [A]*ny other rotary earth-drilling equipment manufactured and sold by TEXOMA during the continuance of this Agreement*, provided, however, that this Sub-section (d) shall not be deemed to apply to or to include such equipment which is the subject of either a bona fide and genuine patent application filed by any third party(ties) or covered by United States Letters Patent owned by TEXOMA or any third party(ies) and

> contains only such other elements or features which are within the public domain. [Emphasis added.]

The contract continues for a period of five years or until three hundred "products" shall be sold or $1,500,000 in commissions paid. During this period Texoma is given the right to an injunction restraining Reich and Paul from competing in the manufacture and sale of rotary drilling machines. The contract further provides that if Texoma should decide to terminate the manufacture and sale of "products" as defined in the contract, it should have no further liability, but must give notice to Reich and Paul, who have the option to require a reassignment to them of all rights under the patent application and any patent issued on it.

After the contract was signed, Reich discontinued his own business and entered the employment of Texoma, which was succeeded by defendant Reed Tool Company. Neither Texoma nor defendant had previously been in the business of making and selling earth-drilling equipment. When Reich's patent application was granted, the patent was issued to defendant as assignee. Defendant made and attempted to sell several of the machines, but according to defendant's evidence, the venture was not a financial success. Defendant then gave Reich and Paul notice that it was terminating manufacture and marketing of the "product." Reich exercised his option to require a reassignment of

the patent, and defendant made such a reassignment. Defendant did not, however, terminate the business of manufacture and sale of earth-drilling equipment. Instead, it undertook the manufacture and sale of another machine, known as the "Stonekiller," on which an earlier patent had expired. Defendant took the position that this machine was not within the definition of "product" in section (1)(d) of the contract. Reich and Paul, on the other hand, asserted that the Stonekiller was within this definition, and they brought this suit to recover commissions on these sales at the rates provided in the contract. Defendant pleaded also that their agreement to make payments on the sale of machines not covered by the Reich patent was a misuse of the patent and of the patent application and, therefore, unenforceable.

1. Misuse of Patent Application

Patent misuse is a doctrine developed by the federal courts to prevent the holder of a patent from using his statutory and constitutional monopoly power to coerce economic benefits not directly flowing from the rights granted by the patent. For example, the holder cannot tie sales of a patented device to purchase of unpatented supplies. Morton Salt Co. v. G. S. Suppiger Co., 314 U.S. 488 (1942). He cannot exact royalties for the use of a patented invention after the patent expires. Brulotte v. Thys, 379 U.S. 29 (1964). Also, he cannot control the resale price of patented products. Straus v. Victor Talking Machine Co., 243 U.S. 490 (1917).

Appellants Reich and Paul contend that the doctrine of patent misuse does not apply to the sale of an application for a patent, as distinguished from the sale of a patent already issued, because until the patent is issued the applicant has no monopoly power subject to abuse. On this question the authorities are inconclusive.

Appellants rely principally on Heltra, Inc. v. Richen-Gemco, Inc., 395 F.Supp. 346 (D.S.C. 1975), *rev'd on other grounds* 540 F.2d 1235 (4th Cir. 1976). *Heltra*, as we view it, does not bear on this point. Although the contract in *Heltra* was similar in some respects to that in this case, the question was not one of patent abuse, but rather whether one who had purchased the rights to an invention, including the rights under a patent application, could deny liability for the purchase money on the ground that the patent, when later issued, was invalid. *Heltra* stands for the rule that in this situation the validity of the patent is immaterial to the purchaser's liability. There was no provision in the *Heltra* contract for payments based on sales of other devices, nor was patent abuse raised as a defense to the suit.

The cases cited by appellee lend some support to appellee's position, though none presented the exact question now before us. Appellee contends that the rationale of the misuse doctrine is equally applicable to agreements involving prospective or inchoate patent rights, such as those flowing from patent applications, as to agreements involving issued patents. It relies on

the test of patent misuse laid down by the Supreme Court in Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100 (1969), and on decisions of federal trial courts and courts of other states. The *Zenith* case concerned issued patents rather than patent applications. Hazeltine owned patents on television sets which it offered for license to Zenith on condition that Zenith pay royalties on all television sets manufactured, regardless of whether any of the inventions subject to Hazeltine's patents were employed. Zenith refused the offer, and Hazeltine sued Zenith for infringing some of its patents. The Supreme Court held in favor of Zenith on its defense that Hazeltine's offer constituted patent misuse. The Court said:

> We hold that conditioning the grant of a patent license upon payment of royalties on products which do not use the teaching of the patent does amount to patent misuse. 395 U.S. at 135. . . . And just as the patent's leverage may not be used to extract from the licensee a commitment to purchase, use, or sell other products according to the desires of the patentee, neither can that leverage be used to garner as royalties a percentage share of the licensee's receipts from sales of other products. In either case, the patentee seeks to extend the monopoly of his patent to derive a benefit not attributable to use of the patent's teachings. 395 U.S. at 136. . . . But we discern

> no basis in the statutory monopoly granted the patentee for using that monopoly to coerce an agreement to pay a percentage royalty on merchandise not employing the discovery which the claims of the patent define. 395 U.S. at 140.

Appellee relies on two state-court cases involving contracts made when applications for patents were pending, but in each the misuse doctrine was held inapplicable under the *Zenith* test because the evidence failed to show that the patent applicant had conditioned his assignment or license or prospective patent rights on payments unrelated to sales of products covered by the patent application. Mutchnik v. M. S. Willett, Inc., 274 Md. 610, 337 A.2d 72 (Md. 1975); Richards v. Liquid Controls Corp., 26 Ill.App.3d 111, 325 N.E.2d 775, 784 (App. Ct. 1975). In *Mutchnik*, the court observed that when the agreement was negotiated, no patent had been issued and at most the licensee's bargaining position was influenced by the existence of the pending patent application.

Appellee relies also on three federal district court opinions. In Key Pharmaceuticals, Inc. v. Lowey, 373 F.Supp. 1190, 1193 (1974), the grantee of an exclusive license to make certain pharmaceuticals according to a process described in a patent application sued to rescind the agreement and was allowed by the court to amend its complaint to add a count alleging misuse in that the licensee was required to pay royalties on specified

products, regardless of whether produced by the processes described in the patent application. The opinion does not discuss application of the misuse doctrine to a patent application, but seems to assume that it would apply if the allegations should be supported by proof.

The other two federal district court cases were patent infringement suits in which the patentees were held disqualified to sue on the ground that they had misused their patents by making license agreements with third parties tending to restrict sales of similar products. Krampe v. Ideal Industries, Inc., 347 F.Supp. 1384, 1386-87 (N.D.Ill. 1972); Anderson Company v. Trico Products Corp., 237 F.Supp. 834, 838 (W.D.N.Y. 1964). In each of these cases the agreements had been made when the application for the patent was pending, but the plaintiff had undertaken to enforce the restriction after the patent had been issued to him. In *Krampe* the court observed that the plaintiff "possessed inchoate rights" in the invention from the time he filed his application and held:

> Accordingly, this Court finds that plaintiff's use of the rights which he possessed in his invention to secure an additional right to which he was not entitled, combined with his maintaining the objectionable terms of the contract after these rights had ripened into a patent monopoly, constitutes misuse of his patent for the cable stripper.

Appellants point out that in the present case, unlike the plaintiffs in *Krampe* and *Anderson*, Reich never owned the patent in question and the parties never contemplated that he would because, by the contract in question, he assigned all his rights under the applications to Texoma, to whose successor the patent was issued pursuant to the assignment. Appellants also argue that there could be no misuse of the monopoly rights granted by the patent in question here because an applicant has no monopoly until the patent is issued, and, since no patent was ever issued to Reich, he could not be guilty of misuse. We do not agree that an applicant who assigns his prospective patent rights can never be guilty of misuse. An inventor who has applied for a patent on a marketable invention may indeed have bargaining leverage to exact benefits he could never get if he did not have a patent application with a fair prospect of success. If he conditions the sale of his prospective patent rights on a promise of payments based on sales of unrelated products, he is using his prospective monopoly power to obtain benefits beyond the scope of his prospective monopoly. He should be in no better position than if the patent had already been issued.

Neither is it essential to the misuse doctrine that the inventor continue to use the leverage of his monopoly after the patent has been issued. If he has obtained a promise of benefits unrelated to the patent on condition of an assignment of his patent rights, whether ac-

tual or prospective, such a promise is within the rationale of the misuse doctrine, as stated by the Supreme Court in *Zenith*. Consequently, we hold in this case that the defense of patent misuse is available, even though Reich had no patent when he sold his invention and his prospective rights under the patent application.

2. *Evidence and Findings of Patent Misuse*

Appellants contend further that even if the misuse doctrine is available as a defense to a suit on a contract made before the patent is issued, no misuse is established by the evidence and verdict in this case. They argue that a fact issue on misuse is made by the evidence in this case, and that appellee failed to obtain a jury finding that would support the judgment in appellee's favor.

We agree with appellants that a fact issue is raised. Appellee's evidence tends to show that Texoma's representatives proposed the contract without paragraph (1)(d), which brings other drilling equipment manufactured and sold by Texoma within the definition of "products" on which commissions must be paid. Appellee's witnesses testified that Reich insisted on this provision and that Texoma agreed to it only because Reich's rights to the invention and his prospective patent rights could not be obtained on any other terms. On the other hand, appellants' evidence tended to show that the patent application was not a primary

item in the negotiations leading to the contract. Appellants assert that appellee was eager to get into the shallow-well drilling equipment business in which Reich was already established, that appellee, through its subsidiary, Texoma, not only bought the invention through its subsidiary, Texoma, not only bought the invention and the patent application from Reich, but took over his business, obtained his services, and secured his agreement not to compete. Thus, according to appellants, it was reasonable and proper for the parties to agree on a consideration that included commissions on sales of equipment, whether or not covered by the claims of the patent application assigned in the contract. In response appellee points out that the contract by which Reich entered appellee's employment and agreed not to compete was a separate transaction supported by an independent consideration, and it insists that the agreement in the contract in question to pay commissions on unrelated products must be taken as part of the consideration for Reich's assignment of his prospective patent rights.

This question is not resolved by the provisions of the contract itself, as both parties agree. In the case of a patent license, it is not *per se* a misuse to measure the consideration by a percentage of the licensee's total sales, including sales of products not within the patent. Automatic Radio Mfg. Co. v. Hazeltine Research, Inc., 339 U.S. 827, 834 (1950). Misuse occurs when the patentee conditions the license on payments based on sales

of other products, and thus uses the leverage of his monopoly to coerce an agreement to make payments based on sales of merchandise not employing the discovery which the claims of the patent define. Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100, 139-40 (1969). Consequently, the negotiations leading up to the contract are relevant to determine whether improper conditioning has occurred, and the party asserting misuse has the burden of proof. Mutchnik v. M. S. Willett, Inc., 274 Md. 610, 337 A.2d 72, 75-77 (1975). Determination of this issue requires a finding of fact. Glen Mfg., Inc. v. Perfect Fit Industries, Inc., 420 F.2d 319 (2d Cir. 1970).

Appellants insist that no such fact finding has been made in this case. The finding on which appellee relies to support its defense of misuse is the following:

> SPECIAL ISSUE NO. 2: Do you find from a preponderance of the evidence that Plaintiff Reich would not have entered into the agreement sued upon if Article (1)(d) thereof had not been included in the agreement?
>
> ANSWER: We do.

Appellants argue that this issue is evidentiary and that the answer is immaterial because the proper issue under *Zenith* and the other authorities above cited is whether appellants conditioned their assignment of patent rights on the payments promised; that is,

whether plaintiffs used their patent power to compel insertion of paragraph (1)(d) in the contract. Appellants bring forward no objection to the issue as submitted. They assert that they had no burden to point out the defect in the issue because the burden was on appellee to obtain a finding establishing the defense of misuse.

We conclude that the issue as submitted and answered is sufficient, in the absence of objection, to support the defense of misuse. Though possibly subject to objection as evidentiary, it was submitted in connection with appellee's plea of patent misuse and gave notice to plaintiffs that an affirmative answer might be taken as a basis for a judgment sustaining that plea. Consequently, appellants were required to point out any defect by a timely objection to the issue. Allen v. American Nat'l Ins. Co., 380 S.W.2d 604 (Tex. 1964). They could not wait until after judgment and then assert that the finding should be disregarded in rendering judgment. Lanphier Const. Co. v. Fowco Const. Co., 523 S.W.2d 29, 43 (Tex. Civ. App. - Corpus Christi 1975, writ ref'd n.r.e.); Panhandle & S. F. Ry. v. Friend, 91 S.W.2d 922, 930 (Tex. Civ. App. - Austin 1936, writ ref'd). A complaint that an issue is evidentiary rather than ultimate is among those that are waived by failure to make a timely objection, and in the absence of such an objection, an issue subject to such a complaint may form the basis of a judgment. Weingarten, Inc. v. Scott, 456 S.W.2d 266, 271 (Tex. Civ. App. - Houston [14th Dist.] 1970, no writ). Although in the cases cited

the courts rested the waiver on the complaining party's failure to make a timely objection, the same rule, in our opinion, applies if an objection is made but is not brought forward on appeal as a ground for a new trial. Consequently, even if appellants objected to the issue in the trial court, they have waived it by not bringing it forward in their brief on this appeal as a ground for a new trial.

Although issue number two may be subject to objection, it bears directly on the defense of misuse. In *Zenith* the concept of "conditioning" a patent license is explained as "where the patentee refuses to license on any other basis and leaves the licensee with a choice between a license so providing and no license at all." 395 U.S. at 135. The same test has been applied to an assignment. Compton v. Metal Products, Inc., 453 F.2d 38, 46 (4th Cir. 1971). The jury found in answer to issue number two that Reich "would not have entered into the agreement sued upon if Article (1)(d) had not been included." This answer is equivalent to a finding that plaintiffs refused to assign their patent application on any other basis and left Texoma with a choice between an assignment containing article (1)(d) and no assignment at all. Appellants have not suggested any additional factual element that should have been submitted to establish that plaintiffs conditioned the assignment on Texoma's promise to pay commissions on sales of products not covered by the claims of the patent application. If any additional finding was

necessary to establish the defense of misuse, such a finding must be deemed to have been made by the trial court in support of the judgment in the absence of objections to failure to submit the omitted component. Rule 279, TEX. R. CIV. P.; Kirk v. Standard Life & Accident Ins. Co., 475 S.W.2d 570, 572 (Tex. 1972); Rogers v. Ellsworth, 501 S.W.2d 756, 757 (Tex. Civ. App. - Houston [14th Dist.] 1973, writ ref'd n.r.e.). No such objection appears in the present record. We hold, therefore, that the answer to issue number two is material, that appellants waived any defect in it, and that the trial judge did properly base his judgment on it.

Affirmed.

/s/ CLARENCE A. GUITTARD
CLARENCE A. GUITTARD
CHIEF JUSTICE

APPENDIX "B"

CLERK'S OFFICE—SUPREME COURT

Austin, Texas

Oct. 24, 1979

Dear Sir:

You are hereby notified that the Application for Writ of Error in the case of REICH ET AL v. REED TOOL CO., No. B-8695, was this day refused. No reversible error.

Very truly yours,
GARSON R. JACKSON, Clerk

Received Oct. 26, 1979

APPENDIX "C"

CLERK'S OFFICE—SUPREME COURT

Austin, Texas

Dec. 5, 1979

Dear Sir:

You are hereby notified that the Motion for Rehearing in the case of REICH, ET AL v. REED TOOL CO., No. B-8695, was this day overruled.

Very truly yours,
GARSON R. JACKSON, Clerk

Supreme Court, U. S.
FILED
APR 11 1980
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

No. 79-1439

WENDELL REICH AND ROBERT PAUL,
Petitioners,

VERSUS

REED TOOL COMPANY,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF TEXAS

RESPONDENT'S BRIEF IN OPPOSITION

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IN THE

Supreme Court of the United States

No. 79-1439

WENDELL REICH AND ROBERT PAUL,
Petitioners,

VERSUS

REED TOOL COMPANY,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF TEXAS

RESPONDENT'S BRIEF IN OPPOSITION

Respondent Reed Tool Company respectfully requests that this Court deny the petition for writ of certiorari, seeking review of the final order of the Supreme Court of the State of Texas. The opinion of the Court of Civil Appeals for the Fifth Supreme Judicial District of the State of Texas (which the Supreme Court of the State of Texas refused to review, stating there was no reversible error) is reported at 582 S.W.2d 549, and a copy is attached to the petition as Appendix "A".

LACK OF JURISDICTION

Respondent respectfully submits that the petition for writ of certiorari should be denied because it was not filed in time. As the petition notes, the Supreme Court of the State of Texas entered its final order on December 5, 1979. Thus, the statute, 28 U.S.C. § 2101(c), requires that the petition must have been filed on or before March 4, 1980. An application by petitioners for an extension of the time in which to file the petition was filed on February 29, 1980 and denied on March 6, 1980. The petition was subsequently filed on March 15, 1980, some eleven days after the statutory deadline. Petitioners' petition for a writ of certiorari was not filed within the statutory time and should be denied for that reason.

QUESTION PRESENTED

Did petitioners misuse their patent rights by conditioning the grant of their patent rights to respondent upon a provision in the agreement requiring respondent to make payments on machines outside the lawful scope of petitioners' patent rights?

STATEMENT OF THE CASE

This is a contract case involving the application of the doctrine of misuse of patent rights. The opinion of the Texas Court of Civil Appeals (reported at 582 S.W.2d 549) is substantially correct in stating the nature and result of the case.

REASONS FOR DENYING THE WRIT

As the opinion of the Texas Court of Civil Appeals (582 S.W.2d 549) points out, petitioners conditioned the grant of their patent rights on a provision of the agreement sued

upon requiring respondent to make payments on machines not within any of petitioners' patent rights or prospective patent rights. The machine upon which payments were claimed, known as the "Stonekiller", is a substantial duplicate of a machine which has been in the public domain since the mid-1950's, long before petitioners made their "invention" in 1970. The Stonekiller was covered by an earlier expired patent. 582 S.W.2d at 551.

Petitioners have cited *no authority whatsoever* in support of the position they urge before this Court. Indeed, all of the authorities support respondent's position.

This Court has long and consistently held that any attempt to extend patent rights beyond their lawful and legitimate scope to gain an economic benefit not attributable to the use of the patent rights constitutes misuse of the patent rights and thereby renders unenforceable any agreement based on such misuse. *Motion Picture Patents Co.* v. *Universal Film Manufacturing Co.*, 243 U.S. 502 (1917), *Carbice Corp. of America* v. *American Patents Development Corp.*, 283 U.S. 227 (1931), *Leitch Manufacturing Co.* v. *Barber Co.*, 302 U.S. 458 (1938), *Morton Salt Co.* v. *G. S. Suppiger Co.*, 314 U.S. 488 (1942), *Brulotte* v. *Thys Co.*, 379 U.S. 29 (1964), *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 395 U.S. 100 (1969). See also *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225 (1964), *Compco Corp.* v. *Day-Brite Lighting, Inc.*, 376 U.S. 234 (1964), *Lear, Inc.* v. *Adkins*, 395 U.S. 653 (1969).

Conditioning an agreement on a requirement that respondent pay on machines not within petitioners' patent rights or prospective patent rights constitutes misuse of those rights and renders the agreement unenforceable, as the Texas Court of Civil Appeals properly held. The rationale of the doctrine of misuse of patent rights applies equally as well to agreements involving prospective or inchoate

patent rights, such as those flowing from patent applications, as to agreements involving issued patents. The policy is to prevent those having prospective patent rights from using them as leverage to extract payments on devices which are in the public domain and not within those prospective patent rights. *Mutchnik* v. *M. S. Willett, Inc.*, 337 A.2d 72 (Md. Ct. App. 1975); *Richards* v. *Liquid Control Corporation*, 325 N.S. 2d 775 (Ill. App. Ct. 1975); *Krampe* v. *Ideal Industries, Inc.*, 347 F.Supp. 1384 (N.D. Ill 1972); *Key Pharmaceuticals, Inc.* v. *Lowey*, 373 F.Supp. 1190 (S.D.N.Y. 1974); *Anderson Co.* v. *Trico Products Corp.*, 237 F.Supp. 834 (W.D.N.Y. 1964).

In *Mutchnik* v. *M. S. Willett, Inc.*, 337 A.2d 72, 75 (Md. Ct. App. 1975), the court said.

> As we understand it, there are two elements in a claim of patent misuse under *Zenith*, namely, conditioning and improper extension of the patent monopoly to cover unpatented products.

The *Mutchnik* court quoted the following language from *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 395 U.S. 100, 136 (1969):

> And just as the patent's leverage may not be used to extract from the licensee a commitment to purchase, use or sell other products according to the desires of the patentee, neither can that leverage be used to garner as royalties a percentage share of the licensee's receipts from the sale of other products; in either case, the patentee seeks to extend the monopoly of his patent to derive a benefit not attributable to use of the patent's teachings.

This Court in *Zenith* held in no uncertain terms that

> conditioning the grant of a patent license upon payment of royalties on products which do not use the teaching of the patent does amount to patent misuse. 395 U.S. at 135.

This case falls squarely within the definition of misuse set forth in *Zenith*. Article (1)(d) of the agreement (quoted at 582 S.W.2d 551) requires respondent to pay on drilling equipment which does not use the teaching of petitioners' patent application or patent, and the jury found that petitioners conditioned the agreement upon this requirement. 582 S.W. 2d at 553-5.

In *Mutchnik* v. *M. S. Willett, Inc.*, 337 A.2d 72 (1975), the Court of Appeals of Maryland, as mandated by *Zenith*, held that an agreement is unenforceable because of misuse where the agreement (an exclusive license) is conditioned upon the requirement that the exclusive licensee shall make payments on devices not within the licensed patent application or subsequently issuing patent. As in this case, *Mutchnik* involves the application by a state court of the doctrine of misuse of patent rights in a factual context wherein the agreement sued upon was entered into during the pendency of the application for a patent. The patent subsequently issued and thereafter a dispute arose with respect to what devices were properly includable within the agreement.

The *Mutchnik* court of appeals reversed the trial court because there was no conditioning as required by *Zenith*. However, in our case, the jury has found conditioning, and *Mutchnik* coupled with *Zenith* compel an affirmance of the lower court's opinion that petitioners take nothing because the agreement constitutes a misuse and is therefore unenforceable.

In *Richards* v. *Liquid Controls Corp.*, 325 N.E.2d 775, 777 (Ill. App. Ct. 1975), the agreement sued upon included the assignment of certain *patent applications* (not issued patents) upon which one or more patents subsequently issued. While implicitly recognizing the applicability of the doc-

trine of misuse in such a situation, the court did not apply it because Richards (the plaintiff-assignor) did not condition the agreement (which was an assignment but which was also referred to as a license by the court) on the payment on the manufacture and sale of similar items which do not embody the subsequently-issued patent. 325 N.E.2d at 784. In this case, the jury found the requisite conditioning with respect to Article (1)(d) which requires payment on the manufacture and sale of similar items (i.e., Stonekillers) on which an earlier patent had expired (582 S.W.2d at 551) and which were thereby in the public domain.

In *Glen Mfg. Inc.* v. *Perfect Fit Industries, Inc.*, 420 F.2d 319, 321 (2d Cir.), cert. den. 397 U.S. 1042 (1970), the Court noted the Supreme Court's reliance on

> the principle that a patentee may not use the power of his patent to levy a charge for making, using, or selling products not with the reach of the monopoly granted by the Government

in *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 395 U.S. 100, 136-137 (1969), and applied that principle in a suit for a breach of an agreement calling for payment on all toilet tank covers (the subject matter of the patent) instead of only on those coming within the scope of the patent. The court remanded the case for a finding on conditioning, an element which the jury has already found in this case. *See also, Beckman Instruments* v. *Technical Development Corp.*, 433 F.2d 55 (7th Cir. 1970), cert. den. 401 U.S. 976 (1971).

Thus, contrary to the position urged by petitioners, the doctrine of patent misuse is equally as applicable to agreements dealing with prospective patent rights, such as applications for patents, as it is to agreements dealing with issued patents. *Mutchnik* v. *Willett*, 337 A.2d 72 (Md. Ct. App. 1975); *Richards* v. *Liquid Controls Corp.*, 325 N.E.2d 775 (Ill. App. Ct. 1975), each of which is discussed above.

In *Krampe* v. *Ideal Industries Inc.*, 347 F.Supp. 1384 (N.D. Ill. 1972), misuse was found in an exclusive license agreement relating to a *pending patent application* because of an anti-competitive provision. The opinion contains an excellent discussion of the effect of entering into a misuse agreement during the pendency of an application for a patent and the subsequent issuance of the patent. The *Krampe* court applied the doctrine of patent misuse to plaintiff's "inchoate rights" and held the subsequently issued patent to be unenforceable.

> These rights included, *inter alia*, that of assigning of rights and licensing under his potential patent, as well as that of collecting royalties for the use of his invention. 347 F.Supp. at 1386-7.

In our case, petitioners exercised their inchoate right of assigning their right to a patent and collecting payments for the use of their invention.

> Thus plaintiff's application clearly was still pending at the time he entered into the contract, thereby affording him the inchoate rights which subsequently ripened into his Letters Patent. 347 F.Supp. at 1387.
>
> Further, as defendant asserts, the contracting parties contemplated plaintiff's patent protection, for the agreement recites that plaintiff is the owner of "protective rights" in the cable stripper. Thus, plaintiff intentionally was using whatever rights he possessed in the product to effect the agreement precluding the sale of competing, nonpatented cable strippers. 347 F.Supp. at 1387.

So, too, in our case, the patent application was pending when the contract was entered into, thereby affording petitioners the inchoate rights which subsequently ripened into their patent. Thus, petitioners in our case were using whatever rights they possessed to effect the agreement

requiring respondent to make payments on competing, non-patented machines (the Stonekillers) not within their inchoate patent rights. The *Krampe* court went on to say:

> Accordingly, this Court finds that plaintiff's use of the rights which he possessed in his invention to secure an additional right to which he was not entitled, combined with his maintaining the objectionable terms of the contract after these rights had ripened into a patent monopoly, constitutes misuse of his patent for the cable stripper. 347 F.Supp. at 1387.

Accordingly, respondent respectfully submits that the state courts properly held that petitioners' use of their inchoate rights to secure an additional right to which they were not entitled, combined with their attempted enforcement of the objectionable provision by making a judicial demand for payments on machines not within their patent rights constitutes misuse of their patent rights.

In *Key Pharmaceuticals Inc.* v. *Lowey,* 373 F.Supp. 1190 (S.D.N.Y. 1974) misuse was found because the exclusive license agreement licensing a pending patent application was not limited to the coverage of the patent application or the subsequently issued patent, a situation indistinguishable from our case.

In *Anderson Co.* v. *TriCo Products Corp.*, 237 F.Supp. 834 (W.D.N.Y. 1964) misuse was found because of a "standardization" clause requiring an anti-competitive use of plaintiff's design. The Court held:

> "In the first instance, by use of its *prospective patent power,* Anderson Co. misused the patent by exacting the" [misusing clause]. 237 F.Supp. at 838; emphasis added.

All of these cases involving an application for a patent (at the time the agreement in suit was entered into) cite

and rely upon misuse decisions, particularly those by this Court, which involve issued patents rather than pending applications. No legal distinction with respect to misuse is or can be drawn between patent rights arising out of a patent application on the one hand and an issued patent on the other hand.

Petitioners urge that the doctrine of misuse of patent rights applies only when there is a license of patent rights, rather than when there is a purported assignment. In our case, the agreement sued upon is rather loosely referred to by petitioners as an "assignment" of patent rights. More precisely, it is a conditional assignment with a contingent right of reassignment and therefore is not an absolute unconditional assignment. The patent in suit is not presently owned by respondent, but was reassigned to petitioner Reich pursuant to the agreement. 582 S.W.2d at 551.

In *Compton* v. *Metal Products Inc.*, 453 F.2d 38 (4th Cir. 1971), the court specifically rejected the very argument which petitioners assert in this case:

> The Special Master found that, "While the patents in suit were part of the assets sold by Joy to Polan, no royalties are payable on the patents as such and, consequently, the agreement does not constitute a patent license agreement but rather a sales agreement and an assignment of all rights under certain patents, tantamount to an assignment of the patents themselves. *Being an assignment of patent rights rather than a license, the rules applicable to misuse as applied to license agreements do not apply.*" • • • *We disagree.* 453 F.2d at 46; (emphasis added).

The court then proceeded to find that the agreement in question constituted a misuse of the patents to which it related.

Thus, with respect to the patent rights granted, be they inchoate or extant, for purposes of misuse there is no practical or legal difference between an exclusive license and an

assignment. In both instances, the licensor and the assignor grant to the licensee or assignee all of the exclusive rights to practice the invention and to prevent others from doing so. These are the so-called "monopoly rights". Neither the licensor nor the assignor retain any right to practice the invention, nor may either grant any rights to any others. Where an application for a patent has been either assigned or licensed exclusively and the patent subsequently issues, the "ripened" patent rights or "monopoly rights" are exercised by the assignee or exclusive licensee *only,* and not by the assignor or licensor. The exclusive licensor keeps bare legal title whereas the true assignor unconditionally passes title without a contingent right of reassignment. For purposes of the application of the doctrine of misuse of patent rights, it matters not who holds bare legal title. Misuse has been applied in both kinds of cases without differentiation or distinction.

The leading case for the proposition that an exclusive patent license is the legal equivalent of a patent assignment is *Waterman* v. *Mackenzie,* 138 U.S. 252, 256 (1891) wherein this Court held:

> Whether a transfer of a particular right or interest under a patent is an assignment or a license does not depend upon the name by which it calls itself, but upon the legal effect of its provisions. *For instance, a grant of an exclusive right to make, use and vend two patented machines within a certain district, is an assignment,* and gives the grantee the right to sue in his own name for an infringement within the district, because the right, although limited to making, using and vending two machines, excludes all other persons, even the patentee, from making, using or vending like machines within the district. (emphasis added)

In *Perry Equipment Corp.* v. *Keller,* 172 U.S.P.Q. 145, 148 (151st Jud. Dist., Harris County, Texas, 1971), the Court concluded as a matter of law:

> An exclusive license to make, use and sell under a U.S. patent is an assignment.

The Court of Claims in *Melin* v. *United States,* 478 F.2d 1210 (1973) held that an exclusive license was an assignment.

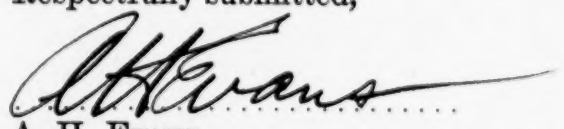
> Although the agreement of December 8, 1964, between Mr. Melin and Rainier was in the form of a license, it granted to Rainier the exclusive right to make, use, and sell the mechanical off-bear and slab-handling apparatus, and, therefore, it was, in substance, a sale or assignment of the entirety of Mr. Melin's rights (if any) in this invention, rather than a mere license. 478 F.2d at 1212.

Thus, petitioners' attempt to avoid the application of misuse because this case involves a conditional assignment is without merit and should be disregarded.

CONCLUSION

For these reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,



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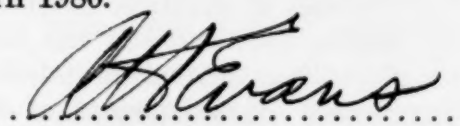
CERTIFICATE OF SERVICE

The undersigned hereby certifies that the foregoing RESPONDENT'S BRIEF IN OPPOSITION was served on petitioners by mailing (certified postage prepaid, return receipt requested) three copies to their counsel of record, Larry Cain, Esq., of Kennedy, Minshew, Evans, Campbell & Cain, Professional Building, Suite 207, Sherman, Texas 75090; this 10th day of April 1980.



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